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1 UNITED STATES DISTRICT COURT  
2 SOUTHERN DISTRICT OF NEW YORK

3 SECURITIES AND EXCHANGE COMMISSION

4 Plaintiff,

5 v.

18 Civ. 8175 (ER)

6 BARRY C. HONIG, et al.,

7 Defendants.

8 -----x  
9 New York, N.Y.  
10 November 7, 2019  
11 4:45 p.m.

12 Before:

13 HON. EDGARDO RAMOS

14 District Judge

15 APPEARANCES

16 NANCY BROWN  
17 JACK KAUFMAN  
18 Attorneys for Plaintiff SEC

19 RICHARD & RICHARD P.A.  
20 Attorneys for Defendants Michael Brauser and Grader  
21 Holdings, Inc.

22 BY: DENNIS RICHARD

23 COOLEY LLP  
24 Attorneys for Defendant Robert Ladd  
25 BY: RANDALL LEE  
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WILMER CUTLER PICKERING HALE & DORR LLP  
Attorneys for Defendant Robert Ladd  
BY: CHRIS JOHNSTONE

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1 (In open court)

2 THE COURT: Good afternoon everyone. Please be  
3 seated.

4 (Case called)

5 MS. BROWN: Good afternoon, your Honor. Nancy Brown  
6 and Jack Kaufman for the plaintiff.

7 THE COURT: Good afternoon.

8 MR. RICHARD: Dennis Richard for the defendants  
9 Michael Brauser and Grander Holdings.

10 MR. LEE: Good afternoon, your Honor. Randall Lee and  
11 Michael Berkovitz from Cooley for defendant Mr. Ladd.

12 MR. JOHNSTONE: Good afternoon, your Honor. Chris  
13 Johnstone of WilmerHale for the defendant Mr. Ladd.

14 THE COURT: And good afternoon to you all. So, this  
15 matter is on for premotion conferences. There are a couple of  
16 requests from Mr. Ladd and one from Mr. Brauser. So, let me  
17 begin with counsel for Mr. Ladd, Mr. Lee.

18 MR. LEE: Thank you, your Honor. There are  
19 essentially two major categories of discovery requests at issue  
20 here. The first is SEC e-mails and documents, which I will  
21 address; and the second are F.B.I. 302s, which Mr. Johnstone  
22 will address.

23 So, on the first sort of category -- and I will go  
24 through the buckets, the first category of requests -- I would  
25 like to briefly address the regulatory background underlying

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1 the purpose for the request, because I think the regulatory  
2 background illustrates the relevance and the importance of the  
3 particular requests that we've made.

4 The essence of the SEC's case against Mr. Ladd and  
5 others arises from Section 13(d) of the Securities and Exchange  
6 Act of 1934, which was adopted as part of the Williams Act,  
7 which was essentially designed to put issuers and market  
8 participants on notice of potential take-over attempts.

9 There is a section in Section 13, Section 13(d), which  
10 requires any "person" who acquires more than five percent of a  
11 class of equity securities to file a form known as a schedule  
12 13(d) upon the acquisition of such ownership. That  
13 requirement, as the language makes clear, applies to any  
14 person. Section 13(d) then provides: When two or more persons  
15 act as a partnership, limited partnership, syndicate or other  
16 group, for the purpose of acquiring, holding or disposing of  
17 securities of an issuer, such syndicate or group shall be  
18 deemed a person.

19 And then there is a rule promulgated under Section  
20 13(d), Exchange Act Rule 13(d)(3), which includes a number of  
21 provisions that define when a beneficial owner of a security,  
22 who that beneficial owner is for purposes of the 13(d)  
23 disclosure requirements.

24 So, for example, Rule 13(d)(3) specifies: When two or  
25 more persons agree to act together for the purpose of

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1 acquiring, holding, voting, or disposing of equity securities  
2 of an issuer, the group formed thereby shall be deemed to have  
3 acquired beneficial ownership of the securities of all the  
4 members of that group.

5 13(d)(3) also goes on to provide, however: That a  
6 group shall be deemed not to have acquired any equity  
7 securities owned by other members of the group solely by virtue  
8 of concerted actions relating to the purchase of equity  
9 securities directly from an issuer, provided that certain  
10 conditions are met.

11 The essence of the SEC's claim here as to one sort of  
12 big chunk of their complaint is that certain of the defendants  
13 led by defendant Barry Honig constituted a group as that term  
14 is defined in Section 13(d), that those investors -- Mr. Honig  
15 and others -- should have filed a schedule 13(d) disclosing  
16 their aggregate holdings as a group, and that our client, Mr.  
17 Ladd and MGT Capital -- the company of which he was CEO -- knew  
18 or were reckless in not knowing that Mr. Honig and the other  
19 defendants were a group and that they should have identified  
20 them as such in their securities filings.

21 And the definition of a group is particularly  
22 important or critical here because Barry Honig -- who has been  
23 described by the SEC as really the orchestrator of the series  
24 of fraudulent schemes that are alleged in the complaint --  
25 Barry Honig did disclose that he was more than a five percent

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1 shareholder. So, the SEC's theory is that he and others should  
2 have together disclosed an even greater percentage of share  
3 ownership than the five percent that Mr. Honig already  
4 disclosed.

5 So, really the reason for our request -- and the  
6 regulatory and statutory scheme should make clear -- the law is  
7 extremely complicated, it's ambiguous.

8 THE COURT: Any case law?

9 MR. LEE: There is case law on it. So, the SEC has  
10 promulgated virtually no guidance -- essentially we are been  
11 able to find -- on how you define a group. There is case law  
12 on it; the case law is mixed. The case law varies.

13 THE COURT: What's the case law in this Circuit? Is  
14 it mixed in this Circuit?

15 MR. LEE: The case law looks essentially at an inquiry  
16 as to whether the alleged or purported members of the group  
17 formed an agreement to vote, dispose of, and so on, their  
18 shares, and it turns into a highly fact-specific analysis. But  
19 for an issuer of securities like MGT, what the SEC has not  
20 explained -- and what the case law we have not been able to  
21 find guidance on -- say absolutely nothing about what the level  
22 of due diligence an issuer is supposed to conduct about its own  
23 investments.

24 So, for example, is it sufficient for an issuer to  
25 rely on representations from its investors if hypothetically

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1 Mr. Honig had informed MGT that he was not part of a group, was  
2 MGT required to look beyond that representation and do its own  
3 due diligence to get behind his representations in the  
4 application of the group? There is no guidance on that from  
5 the SEC, and there is very little case law on that issue as to  
6 whether an issuer is required to look at and do due diligence  
7 at a composition of a group of investors in that issuer.

8 THE COURT: Let me ask it this way: Are there cases  
9 within the Second Circuit or the Southern District that address  
10 the issue that you are talking about?

11 MR. LEE: There may be. Not that I'm immediately  
12 aware of.

13 THE COURT: There may be, and so there may be some  
14 dispositive case out there that I would have to follow, and  
15 would that take of this entire issue?

16 MR. LEE: I would submit that is not the case, because  
17 it's a fact that -- the case law is clear, it's a highly  
18 fact-specific as to whether an agreement was formed. And  
19 that's the essence of sort of the group principle, that  
20 investors who invest side by side with one another, the  
21 presence of a lead investor, investors who share ideas,  
22 investors who say, hey, what are you investing in, that sounds  
23 look a great investment, I would like to do the same thing,  
24 that is not a group. A group requires a specific agreement to  
25 vote together, to dispose of shares together, to buy shares

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1 together.

2 THE COURT: So let me ask this: As I understand it,  
3 what you are looking for are statements of individual SEC  
4 high-level employees or SEC commissioners concerning that  
5 issue, correct?

6 MR. LEE: We're looking for essentially three  
7 categories. Number one is we're asking the SEC to prepare a  
8 privilege log of internal communications concerning the SEC's  
9 application and interpretation of the group rules. The SEC has  
10 declined to produce a privilege log. They have objected on  
11 grounds of relevance; they have objected on grounds of burden.

12 As to relevance, it's plainly relevant to recklessness  
13 and scienter; it's relevant to whether the defendants have a  
14 fair notice defense; and it's relevant to injunctive relief.

15 As to burden, we as recently as yesterday proposed to  
16 the SEC a narrowing of search terms in order to try to generate  
17 a more manageable number. The SEC has claimed that the search  
18 terms we initially discussed yielded 26,000 e-mails, all of  
19 which were ostensibly covered by one single entry in that  
20 privilege log. The SEC said that's too burdensome. We then  
21 had a discussion with them a couple days ago about a proposal  
22 to narrow that, under which proposal if the search term hits  
23 were reasonable in number, the SEC would prepare a  
24 document-by-document privilege log, which would then give us  
25 the ability to challenge the privilege assertions.

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1                   THE COURT: OK.

2                   MR. LEE: We made a proposal to the SEC yesterday, and  
3 we have not heard back from them on a set of search terms.

4                   THE COURT: Ms. Brown?

5                   MS. BROWN: Your Honor, I actually thought this issue,  
6 the latter one we're talking about about the e-mails and the  
7 privilege log, was still under discussion with defendants, so  
8 I'm prepared to discuss it with them.

9                   THE COURT: Great. So, I don't have to engage in this  
10 discussion any further. Next issue.

11                  You should still meet and confer concerning that  
12 issue, and if you don't agree, then you can come back.

13                  MR. LEE: OK.

14                  THE COURT: Okay?

15                  MR. LEE: OK. Next issue was a privilege log of  
16 internal communications within the SEC's Division of Corporate  
17 Finance -- which is the division that reviews public company  
18 filings -- concerning MGT, the very company at issue here. We  
19 asked the SEC -- the SEC has again objected to the notion of  
20 preparing a document-by-document privilege log. In the last  
21 meet and confer we had with them we asked them, well, how many  
22 hits are there; is it unduly burdensome?

23                  THE COURT: So, what you want is documents concerning  
24 internal communications within Corp Fin of MGT.

25                  MR. LEE: About MGT's filings during the relevant time

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1 period.

2 THE COURT: Ms. Brown?

3 MS. BROWN: Yes, your Honor. I also thought that was  
4 the subject of further discussion. But I will say that we also  
5 objected on the grounds of relevance, and it was only yesterday  
6 or the day before -- I may have the days wrong -- in which the  
7 defendant Mr. Ladd offered the relevance ground that it again  
8 was all about the uncertainty within the Commission about the  
9 definition of group under 13(d).

10 So, now that I have that representation, we can come  
11 with search terms related to that narrowed subsection, but  
12 originally it was about all Corp Fin's internal e-mails about  
13 MGT's filings. And MGT's filings aren't at issue here except  
14 with respect to the disclosure of the group issue.

15 THE COURT: OK. So, it sounds like we're making great  
16 progress, just meet and confer some more.

17 MR. LEE: Well, and the other issue that would be  
18 relevant, the other component of the SEC's claim, relates to  
19 certain press release about a deal that MGT entered into with  
20 John McAfee, the internet security guru. So, I think that  
21 would be another set of search terms as to which communications  
22 within Corp Fin, if they had commented on that particular issue  
23 in the course of reviewing MGT's filings, would certainly be  
24 relevant.

25 THE COURT: I'm sorry. How is Mr. McAfee relevant to

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1 this case?

2 MR. LEE: So, the SEC has alleged that MGT made a  
3 false statement in a press release -- which was filed as part  
4 of a form AK -- announcing a deal that MGT had entered into  
5 with John McAfee.

6 THE COURT: The individual.

7 MR. LEE: The individual. And the SEC's allegation is  
8 that the press release described Mr. McAfee's professional  
9 background in a false and misleading manner. And that filing  
10 would have been the subject of internal review in Corp Fin, and  
11 so that's another -- the group rule and then the McAfee press  
12 release are the two sort of substantive issues about which we  
13 would be seeking internal communications if they exist.

14 THE COURT: Ms. Brown?

15 MS. BROWN: That's a new one to me, your Honor. That  
16 was not raised in our call the other day. I am having trouble  
17 understanding how Corp Fin's reaction to a press release would  
18 be relevant to the SEC's later claim that the press release was  
19 false, unless it goes to a claim of laches or estoppel. And  
20 those are not appropriate affirmative defenses against the SEC.

21 MR. LEE: Your Honor, it would certainly be relevant.  
22 It could be. We don't know because the SEC hasn't produced a  
23 privilege log. But if there were comment on the accuracy of  
24 that press release, that could certainly be relevant to Mr.  
25 Ladd's scienter. If, for example, somebody at Corp Fin had

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1 commented, hey, did John McAfee really do this and that, and  
2 somebody else from Corp Fin wrote, you know, no, his background  
3 is a matter of public knowledge, that would be --

4 THE COURT: I have to say I'm having difficulty  
5 following the relevance here.

6 MR. LEE: I'm happy to break it down further, your  
7 Honor.

8 THE COURT: Take a minute to do that.

9 MR. LEE: OK. So the allegation in the complaint is  
10 that MGT falsely stated that John McAfee had sold -- back up.  
11 The backdrop is a deal that MGT and Mr. McAfee are entering  
12 into. The alleged false statement is a statement that John  
13 McAfee, the visionary Internet security pioneer, sold his  
14 company to Intel for \$7.6 billion. That statement was  
15 inaccurate. In truth the company that bore his name was sold  
16 to Intel after Mr. McAfee had already left the company. So  
17 McAfee Associates was in fact sold to Intel for \$7.6 billion.  
18 Mr. McAfee the individual was no longer CEO of the company at  
19 the time it was sold. That's the essence of the SEC's false  
20 statement allegation.

21 THE COURT: I'm sorry. Ms. Brown, how does all of  
22 this fit in?

23 MS. BROWN: I don't know, your Honor. I mean I know  
24 what the false statement is, and I know why we claim it's  
25 false, and I know why we claim it's material, which is that Mr.

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1 McAfee had left McAfee Associates many, many years prior to the  
2 very successful sale of his company. So, our theory is that  
3 the press release was misstated in that way intentionally to  
4 persuade investors that MGT would similarly have bestowed upon  
5 it the magic of Mr. McAfee.

6 MR. LEE: But the fact that Mr. McAfee had left McAfee  
7 Associates was itself a matter of public record. It had  
8 already been publicly disclosed in McAfee Associates' own SEC  
9 filings.

10 THE COURT: So your defense is that it wasn't false,  
11 and if it was inaccurate it was an innocent error?

12 MR. LEE: It was certainly an innocent error. I mean  
13 if you read the language, we have conceded it is technically  
14 inaccurate; he did not personally sell his company. But, as  
15 you say, it's an innocent error, and certainly not material,  
16 and already had been publicly disclosed and therefore it cannot  
17 be an actionable statement.

18 THE COURT: And that is in the complaint against MGT?

19 MR. LEE: That is in the complaint against Mr. Ladd.

20 MS. BROWN: There is no claim against MGT, your Honor.

21 MR. LEE: Against Mr. Ladd.

22 THE COURT: So it's in a complaint against Ladd.

23 MR. LEE: Yes, for having the signed filing that  
24 contained that alleged false statement.

25 THE COURT: OK. So that appears to be somewhat

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1 relevant. Ms. Brown, why don't you give some documents about  
2 that?

3 MS. BROWN: First of all, he is asking for internal  
4 documents. Corp Fin --

5 THE COURT: Well, any documents he is going to ask for  
6 are internal documents, right?

7 MS. BROWN: For today's session, yes, I think.  
8 Actually, no, there is a whole other area that isn't internal  
9 documents.

10 So, what Corp Fin employees said about the filing, I'm  
11 not sure how that relates to Mr. Ladd's innocent mistake or his  
12 intentional false statement. If it's a matter of public  
13 record, that's something that the defendant will prove, I'm  
14 certain, by lots of other evidence. I think that's the subject  
15 of their motion to dismiss. And I just am having trouble  
16 understanding how Corp Fin's internal communications -- if  
17 there are any -- about that filing have any relevance here.

18 THE COURT: Describe for me, if you will, the  
19 relationship between Corp Fin and the Enforcement Division. I  
20 mean that might help me to understand why you think this is a  
21 crazy request.

22 MS. BROWN: Sure. So, Corp Fin is a world unto its  
23 own. We do communicate. When they see things that they think  
24 are troubling, they can make referrals to Enforcement, but  
25 typically what they do is review mostly registration statements

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1 and that kind of thing. Their review of a case -- in fact I  
2 don't even think AKs are filed with the Commission; I think  
3 they're furnished to the Commission, which is a term of art  
4 which does not necessarily require any review. It is simply a  
5 company making a public disclosure, and they furnish it to the  
6 Commission attached to an AK. So, I honestly sitting here  
7 don't know what Corp Fin's view of what its review of those  
8 are, but I suspect it's very limited.

9 Now, again, this was raised for the first time here,  
10 so I'm happy to go ask somebody that question and discuss it  
11 with the defendants further.

12 THE COURT: OK. Do Corp Fin and Enforcement talk?

13 MS. BROWN: Yes. As I said, if Corp Fin sees  
14 something in a registration statement, for example, that they  
15 think is a materially false statement for whatever reason, or  
16 they feel that there is some need for enforcement to take  
17 action, they can make referrals.

18 THE COURT: And are the referrals typically  
19 discoverable or turned over in discovery?

20 MS. BROWN: No.

21 THE COURT: Why not?

22 MS. BROWN: It's part of our nonpublic investigative  
23 process. So until we decide to actually bring an action,  
24 nothing that we do within the SEC's internal processes is  
25 considered public.

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1                   THE COURT: OK. Well, why don't you find out what  
2 there is and let Mr. Lee know what you can. OK?

3                   MR. LEE: That's all we've been asking. At this  
4 stage, in this category, all we're seeking is a privilege log.  
5 And we understand that the issue of whether documents logged  
6 are in fact protected by privilege and is going to be an issue  
7 for another day.

8                   THE COURT: OK.

9                   MR. LEE: The next category -- I mentioned there were  
10 essentially three categories. The next category of documents  
11 that we moved on were statements that SEC officials have made  
12 publicly or to third parties about the issue of the  
13 interpretation or application of the group rules. And the  
14 SEC's response was essentially that there are no such  
15 statements because any statements by an SEC official are made  
16 in his or her own individual capacity; and, number two, that  
17 any public statement or presentation by an SEC official is  
18 publicly available on the SEC's website in any event.

19                   We submit that, number one, clearly SEC officials hold  
20 themselves out as speaking on behalf of the SEC. Not all  
21 public statements include the disclaimer we cited in our reply  
22 brief. A number of aspects are elements of the SEC's own  
23 website which include public statements that are clearly  
24 attributable to the SEC as a whole. And then, number two, it's  
25 not in fact true that all public statements by SEC officials

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1 are posted on their website. SEC officials speak at  
2 conferences, they speak to industry groups, they make public  
3 statements all the time that are not put on the SEC's website.

4 THE COURT: Let me tell you what little information I  
5 have on this topic. I once upon a time was a member of the  
6 Department of Justice, not the SEC, and I spoke on any number  
7 of panels, and I spoke at any number of ADA white collar  
8 conferences, and at each one of those events so did several  
9 dozen others of my DOJ colleagues, and to a person whenever we  
10 spoke we said I'm here in my individual capacity, I do not  
11 speak for the Department of Justice; if you want the Department  
12 of Justice view, go to the Attorney General.

13 And I imagine the way that it's been described to me  
14 that the same is true of the various SEC statements that you're  
15 seeking, that any individual -- and, by the way, there were  
16 also SEC members on some of those panels, and they said the  
17 same thing. And so, therefore, what does it matter what a  
18 particular SEC employee said no matter how high within the  
19 organization, if at the beginning he or she noted I am here not  
20 as a representative of the SEC but as someone that is perhaps  
21 knowledgeable on these issues and I am only giving my own  
22 views? How is that helpful, relevant, admissible, et cetera?  
23 I mean I can see how it's helpful, but how is it relevant or  
24 admissible?

25 MR. LEE: Well, I have several responses. Number one,

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1 certainly the public looks to and market participants look to  
2 statements of at least high-ranking officials, whether it's DOJ  
3 or the SEC, for guidance. That's why they're posted on the  
4 website. If you go to the SEC's website, it's the same as the  
5 DOJ website, at least for a certain category of official, their  
6 speeches are on the website, and not just for idle curiosity,  
7 it's because people look to those statements for guidance, and  
8 people view those statements as being made on behalf of those  
9 agencies notwithstanding the disclaimer.

10 THE COURT: Guidance has a particular definition,  
11 correct?

12 MR. LEE: I beg your pardon?

13 THE COURT: The word guidance in SEC rules has a  
14 particular definition.

15 MR. LEE: No, not necessarily. No, guidance just  
16 means if the chairman of the SEC -- who clearly is somebody to  
17 whom market participants would view as, you know, representing  
18 the SEC's views -- said to an industry group, you know what, we  
19 know that a lot of you are confused by how to apply Section  
20 13(d), that is certainly relevant to our client's scienter, to  
21 recklessness.

22 THE COURT: Right, but that type of comment at that  
23 level within the SEC organization you say is on their website?

24 MR. LEE: Some are, some are not. It is entirely up  
25 to the speaker as to whether they choose to put it on their

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1 website. Not all speakers and presentations are put on the  
2 website. I know that from firsthand experience having been at  
3 the SEC for a number of years. Sometimes they're on the  
4 website, sometimes they're not. Obviously, we can search the  
5 website ourselves. What we have asked the SEC to do is for a  
6 limited number of officials who are authorized to engage in  
7 public speaking -- and it is not a large universe of  
8 individuals; it's individuals at a certain rank -- to search  
9 for speeches on this topic. It's squarely relevant to at the  
10 very least scienter and to recklessness, because the standard  
11 of recklessness is defined as an extreme departure from a  
12 standard of ordinary care, and so the standard of ordinary care  
13 would include what do industry participants view as standard  
14 practice.

15 THE COURT: Ms. Brown?

16 MS. BROWN: So, the limited number of people that Mr.  
17 Ladd suggests we search through, the number of e-mail  
18 custodians at my count currently is 96, and that is  
19 currently --

20 THE COURT: But I guess he is not interested in  
21 e-mails.

22 MS. BROWN: Oh, no, he is, your Honor. He is  
23 interested -- he wants us to search the e-mails of these  
24 individuals for public statements, which I don't know how I  
25 would even guarantee that what is in an e-mail is something

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1 that was actually delivered as a public statement or saw the  
2 light of day.

3                   But on the other side of that is the fact that it  
4 would be extraordinarily burdensome. That's 96 e-mail  
5 custodians today. He has asked for it actually without a date  
6 limitation, but if we applied a reasonable date limitation  
7 that's seven years. I don't know how many multiples of 96 we  
8 would have to search in order to capture everyone who has ever  
9 held the position that he suggested we search for.

10                  THE COURT: I mean it's 96 with no date restriction.  
11 If there were a date restriction it would be fewer, right?

12                  MS. BROWN: No, it's 96 today. So, there are 96  
13 officers, senior officers and division heads that he has asked  
14 for, and commissioner counsel and commissioners. That's 96.  
15 Those people change, so last year it's still 96 but it could be  
16 completely different individuals, and we would have to go get  
17 their e-mails. And then I don't even know that their e-mails  
18 will tell us whether the statements that are contained in there  
19 are actually public statements.

20                  THE COURT: Mr. Lee, that sounds burdensome to me.

21                  MR. LEE: We have not specified that the search for  
22 public statements would need to include an e-mail review.  
23 Certainly the SEC could reach out to -- you know, could make  
24 inquiry of the relevant officials and ask them please provide  
25 us copies of all speeches and public statements you made in the

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1 last X number of years on the topic of Section 13(d).

2 THE COURT: I had to do that when I went through the  
3 confirmation process, find copies of all my public statements,  
4 and it took me the better part of four months, and I'm just one  
5 person. I wasn't doing just that for four months, but I was  
6 putting together the packet, and a lot of it was trying to  
7 figure out when I spoke, where I spoke, what I said, do I have  
8 notes, is there videotape of it, et cetera, et cetera. It is  
9 an incredibly burdensome process to do. You know, there might  
10 be some category of document out there that -- I don't know, I  
11 suppose you could review their website as good as anyone else,  
12 but I don't know how they might limit that search in a way that  
13 would not be burdensome, including upon former SEC officials.

14 MR. LEE: Again, your Honor, I think a couple things.  
15 Number one, I think the vast majority of the so-called senior  
16 officers -- which is the SEC's equivalent of the senior  
17 executive service at the SEC -- they're going to know whether  
18 they have ever given a speech on Section 13 or not. And I am  
19 fairly certain in saying that the vast majority of them have  
20 never given a speech on Section 13. So it's an easy inquiry.  
21 And, number two, this inquiry is no different from the kind of  
22 inquiry that people who prepare deponents for 30(b)(6)  
23 depositions have to go through. You have to make reasonable  
24 inquiry.

25 THE COURT: Yes, but when you a 30(b)(6) deposition

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1 you have an individual or two that's identified as an  
2 appropriate person to give testimony on that particular topic.

3 Look, I think at the end of the day even if we could  
4 formulate -- and again I don't want to carry your water -- but  
5 even if you were to formulate some sort of very limited search  
6 or limited in terms of dates, limited in terms of individuals,  
7 limited in terms of maybe even something less than 96  
8 individuals, that at the end of the day that you're going to  
9 get anything worthwhile, and therefore I find that that  
10 request, given the nature of the case, is too broad, too  
11 burdensome.

12 MR. LEE: The last category -- before we get to  
13 302s -- that we're seeking are additional searches of  
14 communications with third parties by SEC officials about the  
15 application or interpretation of Section 13. This is again a  
16 topic that we discussed a couple of days ago. We made a  
17 proposal. We have not heard back from the SEC on their  
18 response to our proposal as a way to narrow that search. So  
19 even after we filed our motion we continue to engage in a meet  
20 and confer, but the SEC has not responded.

21 THE COURT: OK. Well, respond at some point. OK.  
22 What else?

23 MR. JOHNSTONE: I can speak to the 302 issue  
24 concisely. As you heard from Mr. Lee, the SEC's case revolves  
25 about Barry Honig, who the SEC says orchestrated a fraud

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1 against three public companies. As such, Mr. Honig is the  
2 SEC's central witness in this case. What is interesting is  
3 that he is taking the Fifth, and thus we have no access to his  
4 testimony about what happened.

5 So the parties on this issue have gone through great  
6 lengths to narrow the issues, and it's not a lot of distance  
7 between the two of us. We agree with the SEC -- as they said  
8 in their letter brief -- that an in camera review of its notes  
9 of Mr. Honig's 302s would be an appropriate step forward. The  
10 only question is where should the Court draw the line between  
11 the portions of those notes that should be produced to us and  
12 those that can be withheld.

13 Our request here is very narrow, that the SEC produce  
14 notes of what Mr. Honig said to the government. And we have no  
15 interest in their attorney impressions or anything, ideas about  
16 what he said.

17 So, in drawing the line it's helpful to kind of step  
18 back and understand why the SEC has notes of Mr. Honig's 302s  
19 but doesn't have the 302s themselves. The answer is that the  
20 SEC has gone through great lengths here to keep Mr. Honig's  
21 statements out of this case. They requested review of the  
22 302s. They sat down, they reviewed them, they wrote their own  
23 notes about them. They gave the 302s back to the Department of  
24 Justice and then now are withholding those notes from us.

25 But Mr. Honig's statements about what happened in this

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1 case should be produced. We're not seeking any attorney  
2 impressions, but we have a substantial need for what he said  
3 about what happened, and we have exhausted all other options --  
4 which is an important point. The SEC did not take any  
5 testimony of Mr. --

6 THE COURT: What have you done?

7 MR. JOHNSTONE: First I'll say that the SEC did not  
8 take investigative testimony of Mr. Honig in this case, so we  
9 don't have his statements from that. Second, we served a  
10 subpoena on the Department of Justice, with whom we have met  
11 and conferred, and they have refused to produce the Honig 302  
12 to us. So we have taken that big step, served the subpoena,  
13 meet and conferred with federal prosecutors, and they will not  
14 give it to us.

15 THE COURT: Are there multiple 302s?

16 MR. JOHNSTONE: There is one 302 listed in the  
17 privilege log. I would not be surprised if there are more.

18 THE COURT: OK. What else?

19 MR. JOHNSTONE: Third, we have attempted to depose him  
20 in this case, and we have heard from his attorney that he  
21 intends to assert his Fifth Amendment rights. So, there is no  
22 other option for us to go to get his statements about what  
23 happened in the case. All we are asking for is what the SEC  
24 wrote down about what he said, that's it.

25 THE COURT: Ms. Brown?

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1 MS. BROWN: Yes, your Honor. Mr. Honig hasn't been  
2 deposed yet, so it's news to me that he plans to assert the  
3 Fifth. I did not know that. And I'm not sure any of us know  
4 that until he sits in the chair or he provides the declaration.  
5 That's not to say we shouldn't discuss this issue now.

6 THE COURT: Remind me, is he under criminal  
7 investigation? Has he been indicted? Has he been convicted?

8 MS. BROWN: I've seen no public record of his criminal  
9 status, but he has become a cooperator.

10 THE COURT: So he is cooperating.

11 MS. BROWN: Yes.

12 THE COURT: And you tell me if you -- you know more  
13 about this than I do. In such circumstances if the civil  
14 related matter is not otherwise stayed, do cooperators testify  
15 and give testimony, or do they ask that that deposition be  
16 stayed for some period?

17 MS. BROWN: I think it can vary with the  
18 circumstances. It depends what the status of their cooperation  
19 is. It depends upon the status of their criminal proceeding.  
20 So, if they are sentenced already, they can testify.

21 So -- and I don't have any idea what he is doing to  
22 cooperate, so I don't have much information to share with you.  
23 All I know is he has not yet been deposed.

24 MR. JOHNSTONE: Your Honor, Mr. Honig's attorneys have  
25 represented to us that if he is deposed he will assert his

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1 Fifth Amendment rights, so we know that.

2 THE COURT: OK. And I take it -- again this is more  
3 out of curiosity -- that would not be a violation of his  
4 cooperation agreement.

5 MS. BROWN: I don't know, your Honor. I will say so  
6 that the Court is clear and so the record is clear, that our  
7 notes of 302s -- which themselves as the Court knows are not  
8 verbatim notes of what people say -- are highly selective  
9 material. We go in and we review the 302s, as Mr. Johnstone  
10 just explained, but we don't write down everything that appears  
11 in the 302, we write down what is of interest to us.

12 (Continued on next page)

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1                   THE COURT: Why won't you turn that over?

2                   MS. BROWN: Why wouldn't I turn it over?

3                   THE COURT: Yes.

4                   MS. BROWN: Because it's our work product.

5                   MR. JOHNSTONE: Your Honor, they represented in their  
6 letter brief they would be prepared to submit it in camera. I  
7 think what would be appropriate here is for the SEC to take any  
8 notes that they have taken of the Honig 302 and to highlight  
9 the things that they believe should not be produced because  
10 they are work product, and everything else should be produced  
11 to the defense. Mr. Honig is a significant witness in this  
12 case. If he ever testifies, we need those statements to  
13 impeach him.

14                  THE COURT: If he ever testified, isn't it likely that  
15 you would get those statements at some point; not now, but at  
16 some point?

17                  MR. JOHNSTONE: We don't know. We don't think we  
18 would get them if we were to lose this motion.

19                  Another way to put this is if the SEC were to certify  
20 here today that it will not call Barry Honig and will not  
21 elicit any sort of testimony from him, then we would reconsider  
22 whether we need the notes at all, but we have no visibility  
23 into what the SEC wants us to do, so we need his statements to  
24 impeach him if he ever testifies.

25                  THE COURT: Ms. Brown, out of curiosity, in a criminal

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1 case, certainly once Mr. Honig takes the stand, the 302 gets  
2 turned over, if not shortly before. Does the same thing happen  
3 in civil cases?

4 MS. BROWN: No.

5 MR. JOHNSTONE: Your Honor, it's a very interesting  
6 issue. In criminal cases you're exactly right. Under Rule 16,  
7 302s are produced to the defense, which are grist for  
8 cross-examination in the regular course. You see it here every  
9 day. The SEC has taken the position in cases across the  
10 country that it does into the Brady obligation to provide  
11 exculpatory material in a civil case. This is a civil case.

12 THE COURT: It's more in the nature of Jencks Act  
13 material, not Giglio or Brady. So the statement of any witness  
14 that takes the stand, generally speaking, to the extent that  
15 the notes contain the subject matter of the defendant's  
16 testimony gets turned over. Again, I don't know that the SEC  
17 would have to turn over the 302s because they don't have the  
18 302s, but I don't know that they would be able to withhold  
19 their notes of 302s.

20 Ms. Brown, what is the typical practice, if you know?

21 MS. BROWN: Your Honor, we have long held the position  
22 that our notes of 302s are not producible. They are our notes.  
23 They are our work product. We go to the FBI offices, we look  
24 at the 302s, and we taken down non-verbatim notes of things  
25 we're interested in.

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1                   THE COURT: I take it's SEC attorneys that do that?

2                   MS. BROWN: Yes.

3                   THE COURT: This is an issue upon which it might be  
4 evident that I have very little knowledge about, so it would be  
5 helpful to me in the first instance if the parties were to  
6 submit letter briefs so that when I see the notes in camera I  
7 would have a better idea as to what it is I'm supposed to be  
8 doing.

9                   MR. JOHNSTONE: Your Honor, we're happy to submit a  
10 letter brief on that. We think it makes a lot of sense to  
11 submit the notes in camera so you could see what you're looking  
12 at.

13                   THE COURT: Ms. Brown, any objection to that?

14                   MS. BROWN: No, your Honor.

15                   THE COURT: Mr. Johnstone, correct?

16                   MR. JOHNSTONE: Yes, your Honor.

17                   THE COURT: When do you want to submit your letter?

18                   MR. JOHNSTONE: In a week.

19                   THE COURT: Okay. Next Thursday.

20                   And Ms. Brown, I will give you a week to respond and  
21 submit the letters or the notes in camera. I take it they're  
22 not voluminous.

23                   MS. BROWN: No.

24                   THE COURT: Great.

25                   MR. RICHARDS: Your Honor, may I briefly clarify

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1 something on this issue? So the Jencks Act does not apply to  
2 the SEC.

3 THE COURT: I understand.

4 MR. RICHARDS: And the SEC does not abide by Brady  
5 either. And so to the Court's question, even if Mr. Honig were  
6 to testify in this enforcement action, we would not -- the SEC  
7 would not produce any statements by Mr. Honig, any prior  
8 statements. So that's why we're seeking this in discovery.  
9 It's the only way we can get it.

10 THE COURT: So this is not new news to you that they  
11 would not do that.

12 MR. RICHARDS: Well, it is just we know from the  
13 Jencks Act, it falls under the Federal Criminal Code.

14 THE COURT: I understand that, but I guess my question  
15 is: This has been the SEC's longstanding policy. Presumably,  
16 therefore, they have been doing it for years, judges haven't  
17 made them turn over these materials, and therefore, you are a  
18 petitioner in this area, you should expect that in this case  
19 you will likely also not get these materials.

20 Now I'm learning a lot of this for the first time, so  
21 I'm happy to read up on it, but I understand that criminal  
22 concepts don't apply to SEC proceedings, I was just  
23 analogizing.

24 Okay. So then we'll get your letter in a week,  
25 Mr. Johnstone, and Ms. Brown's response.

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1 MS. BROWN: Are there any replies, your Honor?

2 THE COURT: Do you want to reply, Mr. Johnstone?

3 I don't need a reply.

4 MR. JOHNSTONE: If we believe it's necessary.

5 THE COURT: Very well. Mr. Richard?

6 MR. RICHARD: Yes, your Honor, my issues or my  
7 client's issues are far simpler.

8 THE COURT: I certainly hope so.

9 MR. RICHARD: By way of background, Mr. Michael  
10 Brauser is the subject of claims by the SEC that he essentially  
11 did three things as to all three companies. Number one, he  
12 paid for misleading promotion that artificially increased the  
13 sale of the stock. All of the allegations in the complaint as  
14 to actual payments of named defendants other than Brauser, so  
15 that we're trying to get the evidence of the basis of their  
16 saying that. The second one is that he engaged in matched  
17 trading, which is a term of art, i.e., he put in an offer to  
18 buy stock of each of the three companies, for example, for 75  
19 cents, and there was already another defendant buying it for 75  
20 cents to create an artificial appearance of activity. All of  
21 these 75 cent exchanges that are detailed in the complaint are  
22 between other defendants. So we're looking for the evidence as  
23 to Brauser.

24 The third thing that they're alleging is that Brauser  
25 had an agreement to be part of the group, among whom they

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1 indicate this trading occurred. The SEC's response to our  
2 question and as to what we're seeking in discovery is that my  
3 client's attorney should search through the 4.2 million pages  
4 of documents that the SEC has produced. And their position is  
5 that it's our burden to see if I could find the evidence that  
6 they needed to have under Rule 11 in order to make those  
7 allegations, assuming that they could survive a motion to  
8 dismiss without having -- which is before the Court --  
9 specified those payments and those trades in the complaint.

10 Their position is that they have the right under the  
11 production of electronically stored information, ESI, to merely  
12 present it in the order in which they keep it. However, in  
13 making this argument they're conflating the order in which  
14 documents are kept and how they received the documents. So  
15 what they're actually saying -- they conceded this -- is that  
16 over a period of years we subpoenaed and demanded and asked for  
17 documents from over 200 separate persons and entities, and  
18 those documents came to us in a haphazard fashion. And we're  
19 giving them to you, these four and a half million documents, in  
20 exactly the fashion that we received them, not how we keep  
21 them.

22 Now surely the SEC, in all of the years that they have  
23 had to go through these documents, and we have only had months,  
24 of course, have separated out and organized these documents to  
25 determine what claims they have or the basis for the claims

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1 against each defendant, and specifically the basis of the  
2 claims against Michael Brauser that he paid promoters, that he  
3 engaged in match trades, and that he was part of the aggrieved  
4 group. That's fundamentally what we're looking for.

5 There is a case in this district, in facts it's the  
6 single most comprehensive case in the nation, I think it has 97  
7 footnotes on this very issue, *SEC v. Collins*, where they reject  
8 the SEC's position and they say that you can't just -- and  
9 there I don't think there were 4.2 million documents either.  
10 They say that you can't put on the defendant the burden to find  
11 the evidence that you needed to know under Rule 11 in order to  
12 make the claim, and that you need to be cooperative and you  
13 can't basically hide the ball insofar as the defendant. We're  
14 a single defendant here that does not have the capacity.

15 I know they suggested in their letter brief that my  
16 law firm has the software to somehow search through the 4.2  
17 million documents. We don't. When you're dealing with  
18 documents that are that large, you need substantial major  
19 search engines, which means we have to pay outside vendors to  
20 look through documents, most of which don't have anything to do  
21 with our client.

22 Now what they say is what you asked for are our entire  
23 investigative file, and therefore you got what you asked for.  
24 And I said well, could you tell us which of our 14 or 16  
25 requests these production relate to as to Mr. Brauser. And

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1       their response is we're going to designate them all as  
2       responsive to your request number one, which is the one that  
3       asked for the designated file, and then they stopped sort of  
4       the colon after which there are 14 categories of documents that  
5       we want within their investigative file. So that's basically  
6       what we're looking for.

7               The case in this district, *SEC v. Collins* also points  
8       out that -- and I know that this is still a developing area,  
9       because of the shortfalls of electronic discovery what used to  
10       be a boxcar of documents can now be a hundred boxcars of  
11       documents, and discovery can be weaponized going two ways, both  
12       in a demand and in a production. And essentially it's been  
13       weaponized here in saying that the SEC will not designate in  
14       response to each of our requests.

15               They're pointing to the subsection of Rule 34 on  
16       electronic discovery. What that subsection says and what the  
17       committee notes say is it was an effort to provide the same  
18       production protection to the parties as paper discovery was.  
19       And so basically you can either produce it as kept in the  
20       ordinarily course of business, but also has to be reasonably  
21       determinable as to what the party that is making the request is  
22       looking for. And if not --

23               THE COURT: Let me stop you, Mr. Richard, because I do  
24       at some point have to leave.

25               Ms. Brown, why can't you be a little more targeted

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1 with respect to Mr. Richard's client?

2 MS. BROWN: Well, it's interesting, your Honor, we did  
3 try. So he told your Honor and he told us that the most  
4 important thing was he needed to know where the documents were  
5 that related to our allegation that his clients engaged in  
6 matched trading. We offered to give him the Bates numbers of  
7 those very documents and he declined. So I am happy to  
8 certainly meet halfway with defendant to try to help him find  
9 documents.

10 THE COURT: Did he tell you why he was declining  
11 your --

12 MS. BROWN: Because I said I'm trying to make sure  
13 that we don't actually have to bother the judge with this, let  
14 me give you what you say you really need, which is those  
15 documents, and he declined.

16 I think the reason he declined is because -- and this  
17 is my fear about what he's proposing -- is that this is only  
18 the first of many requests. So, for example, today we have  
19 heard for the first time he wants evidence of our supposed  
20 allegation that his client paid promoters. Well, that's not an  
21 allegation in our complaint. We never alleged that. But it's  
22 a new one that he is suggesting we provide him documents for.

23 So I turn to the rules, because I think it's  
24 important, but I also turn to his own request where he asked us  
25 to produce the documents we had in the form that we kept them,

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1 and that's what we did.

2 THE COURT: So he asked for --

3 MS. BROWN: He asked for --

4 THE COURT: What he's complaining about is precisely I  
5 what he asked for?

6 MS. BROWN: Yes. That asked that we produce ESI in  
7 the form that we maintained them, and that's what we did. In  
8 fact, we told him, consistent with the rules, that we were  
9 producing it in that form in a searchable format.

10 You have not heard him say that all of these documents  
11 are not searchable, because they are. So what I fear here is  
12 that we were turning the rules on their heads to create a  
13 situation where if the producing party has thousands and  
14 thousands and thousands of documents, as I admit we do, then  
15 the other side just gets to throw up their hands and say it's  
16 too expensive for us to look through them, and you tell us  
17 where the documents are that we want.

18 THE COURT: Is it true that the index for this case is  
19 11,000 pages?

20 MS. BROWN: No, it is not. The index I attached to my  
21 letter, your Honor. It was produced by our systems but redone  
22 by me to give them what they wanted, which is a Bates number  
23 range for every single producing party.

24 So for example, if he wanted to know where his broker  
25 was and figure out what those documents were, I invited him to

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1 do that. And let's not forget that I invited him, before he  
2 even made his request, to tell me what he was interested in,  
3 and he chose to serve a request that asked for everything we  
4 have.

5 THE COURT: In the manner in which you --

6 MS. BROWN: In the manner in which we kept them.

7 THE COURT: Mr. Richard, is anything that she said  
8 inaccurate.

9 MR. RICHARD: Virtually everything that she said is  
10 inaccurate.

11 THE COURT: Did she offer to give you the Bates  
12 numbers for the documents concerning -- I forget the particular  
13 issue.

14 MR. RICHARD: With a significant condition, which she  
15 omitted. First she declined to tell me where they were, then  
16 she gave me 20,000 pages that I could look at to find them,  
17 then finally she said that if I agreed to withdraw this letter  
18 motion and not come to this hearing on the other issues and I  
19 just accepted a single matched trade that she was going to show  
20 me, even though it's not on the complaint, then she would show  
21 if to me, but otherwise she would not. So I wouldn't call that  
22 completely accurate.

23 We have served since then two interrogatories within  
24 the rule, and we have also been told they're not going to  
25 answer these interrogatories in which we asked them to identify

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1 the specific Bates numbers of where these matched trades are  
2 and the specific payments of where the evidence -- I know  
3 counsel just said that they did not allege that Brauser made  
4 these payments. I can tomorrow file something with the Court  
5 quoting the page, chapter, and verse where they allege that so  
6 that I just -- we're not seeking a lot here, and what we're  
7 seeking is we have a series of categories of information, all  
8 of which are tied to the allegations in the complaint.

9 THE COURT: Let me ask you this, she said also you're  
10 complaining that you received these materials in the manner  
11 apparently in which the SEC received it, but she says that  
12 that's the way you asked for it. Is that inaccurate?

13 MR. RICHARD: That is inaccurate. What she's doing is  
14 conflating "received" with how they're kept in the ordinary  
15 course, and the cases talk about this, too. We didn't ask for  
16 it as received over the last three years for 220 sources, we  
17 asked for them to show it to us as they keep it.

18 They're not denying that over the years in order to  
19 make the claims against my client they went through all of  
20 these documents, these millions of pages of documents from  
21 these 220 sources and they have organized them in some fashion,  
22 they just want us to have the disorganized fashion that they  
23 received them in over several years. So there's a distinction.  
24 What the rule says is --

25 THE COURT: I get it. I listen very carefully to what

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1 people tell me, and when someone tells me X and other person  
2 tells me Y, I try to determine: Is someone not being  
3 completely truthful or accurate or careful enough? Which is  
4 why I have been going back and forth and asking you very  
5 specific questions about precisely what she said.

6 So let me go to you again, Ms. Brown. How did he  
7 request these documents?

8 MS. BROWN: I'm reading from Exhibit A of my letter to  
9 you, which is their document request, and it says: Unless the  
10 parties agree otherwise, all electronically stored information  
11 shall be produced in the form in which it is kept in its usual  
12 course. And that is how we produced it.

13 I think Mr. Richard doesn't believe me that we keep  
14 the documents according to producing party the way they were  
15 produced to us, but we do. And so we have to search for them.  
16 If we need something, we have to search for them.

17 Your Honor, there's a time and a place for exchanging  
18 trial exhibits and exchanging contention interrogatories, and  
19 I'm happy to talk about that, and to do that at that time, but  
20 this isn't it.

21 THE COURT: Okay. Your request is denied,  
22 Mr. Richard.

23 I think that's it. I need to go. We're adjourned.

24 MS. BROWN: Thank you.

25 MR. RICHARD: Thank you.